UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

AMERICAN ELECTRIC POWER COMPANY, INC.

Administrative Proceeding
File No. 3-11616

NARRATIVE SUMMARY OF THE CASE SUBMITTED BY AMERICAN ELECTRIC POWER COMPANY, INC.

On August 30, 2004, the Securities and Exchange Commission ("Commission") issued an order requiring a hearing in this matter "for the purpose of determining whether the AEP and CSW systems are interconnected and operate in the same area or region[.]" This narrative summary is submitted on behalf of American Electric Power Company, Inc. ("AEP"), and summarizes AEP's statement of its case with respect to the two issues that remain before the Commission.[1]

On January 18, 2002, the United States Court of Appeals for the District of Columbia Circuit in *National Rural Electric Cooperative Association v. SEC*, 276 F.3d 609 (D.C. Cir. 2002) ("*NRECA v. SEC*") remanded the Commission's approval of the merger of AEP and Central and South West Corporation ("CSW"). In its decision, the Court found that the Commission had failed to explain adequately certain of its conclusions under the Public Utility Holding Company Act of 1935 (15 U.S.C. § 79 *et seq.* (2000) ("Act"). Specifically, the Court determined that additional findings are required with respect to the statutory requirements that an "integrated public-utility system" be: (i) "physically interconnected or capable of physical interconnection" and (ii) "confined in its operations to a single area or region." *Id.* at 614 and 618 citing Section 2(a)(29)(A) of the Act. With the evidence AEP now proposes to add to the existing record, substantial evidence will exist in the record to support all aspects of the Commission's decision to approve the merger, including its findings on

[1] In addition to presenting the evidence described in this Narrative Summary, AEP may wish to submit evidence responding to the positions advanced by intervenors in their Narrative Summaries, which are due to be filed on November 30, 2004. AEP respectfully reserves the right to submit such additional evidence with its testimony on December 3, 2004.

"interconnection" and "single area or region." So long as the Commission fulfills its duty to explain and justify its decision in a manner consistent with the Court's analysis, its interpretation of the statute, in light of the evidence, is entitled to the deference afforded by the *Chevron* line of cases.[2] AEP submits that the Commission's initial decision should be reaffirmed, and that express findings should be made to supplement its prior analysis on these two points.

Background

In the *NRECA v. SEC* decision, the Court was reviewing the Commission's order approving the acquisition by AEP of the securities of CSW and related transactions under the Act. *American Electric Power Co.*, Holding Co. Act Release No. 27186 (June 14, 2000) ("Order"). The Order went into immediate effect on June 14, 2000 and, pursuant to the Order, the merger was completed on June 15, 2000 ("Merger"). During the eighteen months that the matter was pending on appeal, AEP and its subsidiaries operated as members of a registered holding-company system ("Combined System") under the Act, and are continuing to so operate.

In its decision, the D.C. Circuit upheld the Commission's determination under Section 10(c)(2) of the Act that the Merger would serve the public interest by tending "towards the economical and efficient development of an integrated public-utility system" by, among other things, producing cost savings of approximately $2.1 billion. *NRECA v. SEC* at 613. The Court, however, agreed with petitioners that the Order did not adequately explain the Commission's conclusion under Section 10(c)(1) – that the proposed Merger would not be "detrimental to carrying out the provisions of Section 11." *Id.* at 610.

As explained more fully herein, the evidence of record, together with the additional evidence AEP intends to provide, will establish an ample basis for the Commission's findings under Section 10(c)(1) and, by reference, Section 11.[3] The legislative history of the Act explains that "the purpose of section 11 is simply to provide a mechanism to create conditions under which effective Federal and State regulation will be possible." S. Rep. No. 621, 74th Cong., 1st Sess. 11 (1935). In this regard, Section

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[2] *See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984); *Madison Gas & Elec. Co. v. SEC*, 168 F.3d 1337, 1339 (D.C. Cir. 1999).

[3] It is also worth noting that the D.C. Circuit has held that the Act requires something less than strict compliance with the standards of Section 11 in the Commission's determinations under Section 10. *See Madison Gas & Electric Co. v. SEC*, 168 F.3d 1337, 1342-43 (D.C. Cir. 1999) ("By its terms, however, section 10(c)(1) does not require that new acquisitions comply to the letter with section 11. In contrast to its strict incorporation of section 8 (proscribing approval of an acquisition 'that is unlawful' thereunder), with respect to section 11 section 10(c)(1) prohibits approval of an acquisition only if it 'is detrimental to the carrying out of [its] provisions.'").

1(b)(4) of the Act identifies, among the problems the statute was intended to address, that:

> the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be adversely affected -- *when the growth and extension of holding companies bears no relation to economy of management and operation or the integration or coordination of related operating properties.* (Emphasis added).

To that end, Section 11(b)(1) requires that the Commission limit the operations of a registered holding company to "a single integrated public-utility system," which is defined as it relates to electric utility operations as:

> a system consisting of one or more units of generating plants and/or transmission lines and/or distributing facilities, whose utility assets, whether owned by one or more electric utility companies, are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation.

Section 2(a)(29)(A) of the Act.

With respect to the requirements of Section 2(a)(29)(A), the petitioners did not challenge the Commission's findings that the AEP electric utility operations would, post-Merger, "be economically operated as a single interconnected and coordinated system," and that the Combined System would not be "so large as to impair . . . the advantages of localized management, efficient operation, and the effectiveness of regulation."[4] The petitioners, however, argued and the Court agreed that the Commission's decision was lacking in two respects.

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[4] Nor did the petitioners challenge the Commission's findings under Section 10(b)(3) that the proposed merger would not be detrimental to "the public interest or the interest of investors or consumers or the proper functioning of such holding-company system."

(1) The Commission failed to provide a "satisfactory explanation" in the Order for its determination that the proposed merger met the statutory requirement that the system be "physically interconnected or capable of physical interconnection" *NRECA v. SEC* at 616; and

(2) The Commission "failed to make any evidentiary findings" or to support separately its conclusion that the resulting system would be "confined in its operations to a single area or region" *Id.* at 617.

Based on these conclusions, the Court remanded for further proceedings "consistent with this opinion." *Id.* at 619.

Narrative Summary of AEP's Case

1. Scope of the Remand.

While the Court directed the Commission to address the "interconnection" issue, the scope of that question is narrowly defined. Importantly, the Court affirmed the Commission's basic conclusion that contract rights may suffice to meet the "physical interconnection" requirement and agreed with the Commission that a 250 MW path provides a sufficient power flow to satisfy the statute. *Id.* at 614-15. The issue with respect to interconnection on remand is, first, whether a "unidirectional flow of power from one-half to the other" of the system can meet the "integration" requirements. *Id.* at 615. Second, the Court directed the Commission either to explain why the Order is consistent with the Commission's "own prior reasoning regarding interconnection of distant utilities" or to provide a "reasoned analysis indicating that prior policies and standards are being deliberately changed" and why that change is legitimate. *Id.* at 615.

The other "remanded" issue is that of "single area or region." Here the Court acknowledged that there may be a "legitimate basis" for finding AEP's service territories and CSW's service territories to be in the same "area or region." *Id.* at 618-19. It found, however, that the Order "failed to justify its finding that the proposed acquisition will satisfy the single-area-or-region requirement." *Id.* at 610.

The Commission's order of August 30, 2004 requiring a hearing in this matter is narrowly tailored to limit the hearing to the foregoing two issues and effectively tracks the Court's own description of their scope.

2. Interconnection

The Merger meets the statutory criterion that utility assets be "physically interconnected or capable of physical interconnection." While the petitioners originally raised numerous objections with respect to this criterion based on the proposed use of a contract path as the primary means of interconnecting the former AEP and CSW systems, most of these objections were rejected by the Court.

The Court's concerns with respect to interconnection were directed only to the Commission's acceptance of a "unidirectional contract path," and to the Court's view that the Commission had failed adequately to distinguish prior precedents which suggested that a contract path might not suffice to integrate "distant" systems. *Id.* at 615-16. Each of these is addressed below.

a. Unidirectional Flow of Power.

The Court focused on the statutory term "interconnection," which it found to connote "*mutual* connection," a definition "that seems, on its face, to require two-way transfers of power." *Id.* at 615. The Court added that it failed to see how a system restricted to a "unidirectional flow of power from one half to the other" could be operated as a "single 'interconnected and coordinated' whole". *Id.* citing Section 2(a)(29)(A) of the Act.

AEP has shown and will provide additional evidence that the Combined System is not simply connected by a "unidirectional flow of power" but in fact has the capability for "two-way transfers of power," which it can and does use to the full extent such transfers may be necessary and economic. Although it is true that the firm contract path ("Contract Path") is from east to west (consistent with the historical and likely future power needs of the system), this firm reservation also includes the option for AEP to reverse the flow from west to east on a non-firm basis at any time at no additional charge. The existence of the Contract Path further provides AEP the option to reverse the flow from west to east on a firm basis but, as expected, there has been little need for west to east capacity since the Merger in 2000.

In addition to the reversibility of the Contract Path, there are other means of transmitting power (or of interconnecting utility assets). In its initial order, for example, the Commission noted that:

> In addition to the use of the Contract Path, quantities in excess of 250 MW may be moved within the New AEP System in any given hour by using non-firm transmission rights. These additional transfers will be made when they would be economical for New AEP System operations, after taking opportunity costs into consideration.

Applicants also expect that, from time to time, there will be opportunity to transfer energy economically from the West Zone to the East Zone. In these circumstances, Applicants will make use of their rights to nominate secondary points of receipt and delivery under their transmission service agreements with Western Resources and Ameren.

Order at 37. While these findings were made in the context of addressing the separate statutory requirement that the proposed system be capable of "economic and coordinated operation," the Court's opinion itself recognizes that these two requirements are related, *NRECA v. SEC* at 615, and that the Commission's findings that there are non-firm avenues for transmitting power in both directions, in addition to the one-way contract path for firm transmission, are directly relevant to the "interconnection" requirement.

Moreover, AEP points out that the Commission has increasingly looked to the use of open access transmission service under FERC Order No. 888[5] as a means of interconnecting utility assets. The Commission noted in its original decision, but did not rely upon, the "efforts of the FERC to restructure the way in which transmission is provided and obtained in the U.S.," which includes FERC's Order No. 888 mandating open access to FERC-jurisdictional transmission facilities. Order at n.59. Since that time, FERC's open access transmission service regime has been more fully realized. Through these open access transmission requirements, the distinction between contract rights and ownership rights to use interstate transmission has been minimized and AEP has used FERC's open access regime to transmit power west to east as well as east to west. AEP will provide further evidence of transfers on a non-firm basis when it has been economically viable.

Under FERC Order No. 888, FERC-jurisdictional utilities have the legal right to purchase available transmission capacity from other FERC-jurisdictional utilities on non-discriminatory terms. Utilities and, as discussed later, regional transmission organizations ("RTOs") have implemented Order No. 888 and FERC's companion Order No. 889[6] by adopting open access transmission tariffs ("OATTs") and posting available

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[5] *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996), FERC Stats. and Regs. ¶ 31,036 (1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 12,274 (March 14, 1997), FERC Stats. & Regs. ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 ("Order No. 888").

[6] *Open Access Same-Time Information System (Formerly Real-Time Information Networks) and Standards of Conduct*, Order No. 889, 61 Fed. Reg. 21,737 (May 10, 1996), FERC Stats. & Regs. ¶ 31,035 (1996), *order on*

transmission capacity on a publicly-available open access same-time information system ("OASIS"). OATTs afford utilities, such as AEP, the same right to purchase available transmission capacity on non-discriminatory terms as the facilities' owner enjoys, and OASIS makes the availability of transmission capacity transparent to potential purchasers and easy to acquire.

The Commission has already recognized the importance of Order No. 888 in the interconnection context:

> [Order No. 888 means that] transmission users no longer need to build their own transmission lines or lease them from third parties in order to secure reliable transmission capacity. Indeed, the primary purpose and effect of Order No. 888 is to give transmission users rights of access to third party facilities that are on a par with the rights of the transmission owners. Consequently, transmission users do not need to buy more transmission than they need to support specific transactions.[7]

In light of this fundamental change in the regulatory requirements applicable to electric power transmission, it is important for the Commission to continue to adapt its approach to interpreting the statutory "interconnection" requirement. As the Commission has recognized, were it to require firm, two-way transmission contracts in every proposed merger under the Act between two non-contiguous systems, it would force utilities to purchase firm transmission that is unnecessary and uneconomic while unnecessarily increasing costs to consumers. Such a requirement would needlessly limit the flexibility and consume the resources of such utilities and "could constrain parts of the grid, to the detriment of other potential transmission users."[8]

Consistent with this reasoning, since the advent of FERC's open access regime under Order No. 888, the Commission has held that non-contiguous utilities can show interconnection through adequate available transmission capacity under intervening utilities' OATTs.[9] This development is the natural extension of the Commission's prior

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reh'g, Order No. 889-A, 62 Fed. Reg. 12,484 (March 14, 1997), FERC Stats. & Regs. ¶ 31,049 (1997), *order on reh'g*, Order No. 889-B, 81 FERC ¶ 61,253 (1997) ("Order No. 889").

[7] *CP&L Energy Inc.*, Holding Co. Act Release No. 27284, at n.25 (Nov. 27, 2000).

[8] *Id.* Such a requirement would also be inconsistent with FERC transmission policy, which is designed to minimize or eliminate hoarding.

[9] *See CP&L Energy, Inc.*, Holding Co. Act Release No. 27284 (Nov. 27, 2000) (concluding that a firm contract path is unnecessary to show interconnection between two non-contiguous parts of a utility system where adequate transmission is available through open access, using the OATTs of other utilities and OASIS, and through other transmission arrangements); *Exelon Corp.*, Holding Co. Act Release No. 27256 (Oct. 19, 2000) (determining that a

"interconnection" decisions, in which the Commission has adapted its interpretation of the statutory language in light of technological and regulatory developments in the field.[10] In *CP&L Energy*, the Commission approvingly recited the applicants' explanation as to why open access transmission "offers a better, more flexible and more economical way to achieve significant interchange capability than the more traditional firm contract path":

> Open access transmission makes it possible now for the [non-contiguous areas of the Carolina Power & Light Company system] to coordinate their operations through the use of OATTs and OASIS . . . [Applicants] explain that reliance on numerous transmission service reservations increases the number of potential interconnection options and allows utilities to use less expensive non-firm products where appropriate, while providing a high level of assurance that transmission capacity will be available when needed. Utilities can obtain a portfolio of transmission capacity over multiple paths, with various degrees of firmness, providing for various amounts of capacity that can be selected to

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combination of a 100 MW firm contract path in one direction and adequate available transmission capacity in the other direction sufficed to interconnect PECO and Commonwealth Edison).

[10] In its very early cases, the SEC indicated that it would require non-contiguous operating companies to interconnect through their own transmission lines, *see, e.g., The North American Co.*, Holding Co. Act Release No. 3405 (1942), but the SEC soon amended this narrow view, holding that the right to use a third party's transmission lines also satisfied the interconnection requirement. *See Cities Serv. Power & Light Co.,* 14 S.E.C. 28, 53 n.44 (1943); *Electric Energy, Inc.*, 38 S.E.C. 658, 668-671 (1958); *New England Elec. Sys.*, 38 S.E.C. 193, 198-99 (1958); *Centerior Energy Corp.*, Holding Co. Act Release No. 24073 (Apr. 29, 1986); *Northeast Utilities*, Holding Co. Act Release No. 25221 n.75, 50 S.E.C. 427 (Dec. 21, 1990); *Conectiv Inc.*, Holding Co. Act Release No. 26832 (Feb. 25, 1998); *WPL Holdings, Inc.*, Holding Co. Act Release No. 26856, 53 S.E.C. 501 (Apr. 14, 1998). This change in interpretation has been approved by the Court. *See Madison Gas & Elec. Co. v. SEC*, 168 F.3d 1337, 1340 (D.C. Cir. 1999).

During the 1950's and 1960's, the Commission further developed its interpretations, holding that a generating plant and its sponsoring companies could be interconnected through a "transmission grid," *Connecticut Yankee Atomic Power Co.,* Holding Co. Act Release No. 14968, 41 S.E.C. 705 (Nov. 15, 1963), or a "transmission network," *Yankee Atomic Elec. Co.*, 36 S.E.C. 552 (Nov. 25, 1955). The Commission also decided that non-contiguous companies could show interconnection without the ability to transfer unlimited amounts of power over a third party's line, at least where they can supplement power transfers through potential transmission contracts with other parties. *Mississippi Valley Generating Co.,* 36 S.E.C. 159 (1955). By the 1970's, when utilities were voluntarily forming regional associations to improve reliability and economy of power supply, the Commission reacted to this change in the industry by relying on transmission agreements among members of the regional associations to find interconnection. *See, e.g., Conectiv, Inc.*, Holding Co. Act Release No. 26832 (Feb. 25, 1998); *Unitil Corp.*, Holding Co. Act Release No. 25524 n.29, 50 S.E.C. 961 (Apr. 24, 1992); *Centerior Energy Corp.*, Holding Co. Act Release No. 24073, 49 S.E.C. 472 (Apr. 29, 1986). The Commission's recent decisions recognizing open access transmission rights as a means of "interconnecting" non-contiguous utility systems are the natural extension of these decisions in the current regulatory context.

> achieve optimal integrated operations. Today, interchange capacity can be achieved via a portfolio of short-term firm and non-firm transmission at a lower comprehensive cost than the more limited, rigid, single firm contract path.[11]

This construction of the statute, which takes into account the current regulatory, business and technological conditions in the industry, is entitled to deference from the courts. *See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984); *Madison Gas & Elec. Co. v. SEC*, 168 F.3d 1337, 1339 (D.C. Cir. 1999).

AEP will present testimony and exhibits that support the foregoing analysis. Such evidence will document the volume of energy transferred from west to east in the Combined System using non-firm transmission capacity. AEP will further supplement the record with additional evidence regarding the availability of capacity for the transmission of power and energy from west to east in the Combined System when it is economical for AEP to do so.

Based on all of this evidence – including the Contract Path for firm transmission, the reversibility of the Contract Path, the availability of non-firm transmission options and rights to use the open access transmission system – the two parts of the Combined System are "physically interconnected or capable of physical interconnection" within the meaning of the Act, including the capability for "two-way transfers of power." *NRECA v. SEC* at 615.

b. Consistency with Prior Precedents.

The Commission's decision in this case is consistent with the Commission's past precedents. In finding an "apparent conflict," the Court cited prior decisions in which the Commission had suggested that "contract rights cannot be relied upon to *integrate* two *distant* utilities," and perceived a failure on the Commission's part to provide a "reasoned analysis indicating that prior policies and standards are being deliberately changed." *NRECA v. SEC* at 615 (emphasis added). The Court appeared to accept the Commission's premise that the length of a contract path was relevant not to the question of *interconnection* but rather to the determination whether interconnected utilities met the "single area or region requirement" (each being a separate element to prove integration). The Court noted, however, that the Commission had "failed explicitly to consider the length of the contact path in deciding whether New AEP meets the region requirement." *Id.* at 616.

[11] *CP&L Energy Inc.*, Holding Co. Act Release No. 27284 (Nov. 27, 2000).

To the extent *dicta* in earlier decisions suggest otherwise, the distance between utility assets is not a legal limitation with respect to satisfying the "interconnection" requirement of the statute. The Commission correctly concluded that distance is a factor to be taken into account only in the context of the "single area or region" requirement and, as discussed more fully herein, AEP will present additional evidence sufficient to make express findings that the Combined System satisfies this requirement. Alternatively, the Commission should disavow its prior dicta suggesting that contract rights cannot be used to interconnect distant utilities, because this dicta is inconsistent with technological changes in the electric industry and with new regulatory policies implemented during the past decade. As discussed above, the FERC has issued Order No. 888 for the explicit purpose of creating comparability between ownership and contract rights to transmission. In addition, the FERC has removed barriers to transmitting power over long distances through its RTO policy, which eliminates "rate pancaking" associated with transactions across multiple utility systems. Finally, a transmission infrastructure now exists that permits power transactions to take place across long distances, and such long distance transactions are now commonplace.

In any event, AEP will present evidence showing that the distance between the facilities of the pre-Merger AEP and CSW is less than the reported distance between Southwestern Public Service Company ("SPS") and Public Service Company of Colorado prior to the 1997 New Century Energies, Inc. merger (300 miles)[12]; between Northern States Power Company, Inc. and SPS prior to the 2000 Xcel Energy Inc. merger (500 miles)[13]; between Carolina Power & Light Company and Florida Power Corporation prior to their merger (350 miles); and between PECO Energy and Commonwealth Edison Company prior to their merger (at least 400 miles).[14] Even paying homage to the *dicta* from older Commission decisions that refer to "distant" utilities, there is no basis for finding that AEP and CSW were "distant" from one another for purposes of the Act.

Accordingly, the Commission's finding that AEP/CSW may be integrated using a contract path reflects a reasonable reading of the statute, is consistent with its prior precedent allowing the formation of other holding company systems interconnected by contract over much greater distances than the AEP/CSW system, and properly reflects the current regulatory, commercial and technological state of the industry.

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[12] *New Century Energies, Inc.*, Holding Co. Release No. 26748 at 11, 53 S.E.C. 54 at 59 (Aug. 1, 1997).

[13] Application of New Century Energies, Inc. on Form U-1, Amendment No. 4 at n.72 (File No. 70-9539) (Aug. 16, 2000).

[14] CP&L Energy, Inc. Holding Co. Release No. 27284 at 40 (Nov. 27, 2000).

3. *Single Area or Region.*

a. *The "Single Area or Region" Requirement as a Separate Element in the Definition of "Integrated Public-Utility System".*

The Court acknowledged that the Commission "may make its own decision regarding the meaning of the region requirement" and that while "the Commission could potentially point to boundaries identified by NERC or FERC" it is not bound by the regions or areas defined by other entities.[15] *NRECA v. SEC* at 617. Further, the Court "accepted as true" the Commission's statements that "the terms 'area' and 'region' are 'by their nature . . . susceptible of flexible interpretation," and that "'recent institutional, legal and technological changes have reduced the relative importance of geographic limitations' on utility systems." *Id.* at 617-18 (citation omitted). However, the Court held that the Commission had not satisfactorily explained the application of these standards to the facts at hand.

Specifically, the Court criticized the Commission's "single area or region" determination as having relied on a finding that "New AEP satisfies all other PUHCA requirements," rather than having analyzed the "single area or region" requirement as a separate element necessary to satisfy the definition of an "integrated [electric] public-utility system" in Section 2(a)(29)(A). *Id.* at 618. The Court also found that the Commission "failed to make any evidentiary findings on the issue", and cited two older Commission decisions[16] in which it described the Commission as having "analyzed such factors as the geography and socioeconomic characteristics of the areas covered by the system." *Id.* at 617. In contrast, the Court asserted, the Commission's decision in this case had not relied on "any identified similarities between the areas currently served by AEP and those served by CSW", and "[n]ever mention[ed] whether the territories served by AEP and CSW have common geographic and geologic traits." *Id.* at 617-18.

The Commission has rarely had occasion in recent years to discuss the "single area or region" requirement as a separate factor in great detail. As a result, while the Court and other commentators frequently reference the discussion of the "single area or region" requirement in the 1944 and 1945 *Middle West* orders, some of the factors

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[15] This approach only makes sense. Were the Commission required to divide the country into set geographic regions – for example, by adopting the petitioners' suggestion that the Commission limit itself to the specific geographical boundaries developed by regional power pools – even contiguous systems that were closely interconnected could be deemed not to operate in a "single area or region" if they happened to fall on two sides of an arbitrary geographic line. Such a reading would make no sense, and the Court agreed that the Commission rightly rejected any such approach as controlling its determinations.

[16] *Middle West Corp.*, Holding Co. Act Release No. 4846, 15 S.E.C. 309, 336 (1944); *American Natural Gas Co.*, Holding Co. Act Release No. 15620, 43 S.E.C. 203, 206 (1966).

relied upon in those dated orders have been trumped by other factors that today have greater relevance to satisfying this requirement. As explained below, however, important elements of these orders continue to be pertinent today.

In the 1944 *Middle West* order, the Commission considered whether to permit the utilities in each of two parts of what later became the CSW system to remain together under Section 11.[17] In discussing the "single area or region" requirement, the Commission acknowledged the large size of the territory, that it was not "well-settled" or "economically developed" and that it was "more or less typical throughout, relying largely on oil and other minerals, agriculture, and relatively light industry for its subsistence." *Id,* at 336. The key, however, to the Commission's finding that the single area or region requirement was satisfied appeared to be the need to provide "satisfactory service":

> The rendition of satisfactory service in arid and sparsely-settled areas frequently requires the stretching of lines over long distances to connect small population centers with generating facilities strategically placed near suitable water and fuel supplies. In view of these facts, we believe that the properties in question lie within a single area or region.[18]

The second set of companies considered in the 1944 *Middle West* order consisted of utilities situated in what the Commission described as an "enormous territory." *Id.* at 337. Again, the Commission viewed the "sparse settlement" of the area, "the difficulties of finding suitable generation locations because of water and fuel characteristics, the small size of communities widely separated and the necessity of stretching lines over long distances to accumulate load" as justifying a finding that the territories constituted a single area or region. *Id.* In the 1945 *Middle West* order, the Commission decided that the two groups could remain in a single system, discarding the tentative conclusion it had stated in the 1944 order.[19] In doing so, it emphasized the factors that would make for success in operating an integrated utility system:

> In our prior opinion we discussed the size and geophysical conditions of the territory. The territory is a large one. However, as we have noted, it is unique in various respects. Limited supplies of adequate water, small and scattered

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[17] *See Middle West Corp.*, 15 S.E.C. 309, 334-35 (1944).

[18] *Id.*

[19] *See Middle West Corp.*, 18 S.E.C. 296 (1945).

> population localities, the generally dispersed industrial and agricultural locations require high concentrations of generating capacity and long transmission lines. Neither localized management nor efficient operation nor the effectiveness of regulation . . . is impaired . . . particularly in light of demonstrated disadvantages of lack of coordination in this case.

Id. at 299. It was not "homogeneity" as such, but the ability to render service, to manage the combined system effectively and the loss of coordination benefits if the companies were not kept together, that seemed to influence the Commission's decisions most heavily, both in 1944 and 1945.[20] The continued significance of these considerations remains, notwithstanding the changed demographics and socio-economic development of that region. In particular, the ability to render efficient and economic service over increasingly greater distances has improved markedly since these orders were issued.

The evidence to be submitted by AEP provides an ample basis for finding the Combined System operates in a single area or region (and not merely because the other three requirements of an "integrated public-utility system" have been met). There are two considerations that should be emphasized in this connection.

First, Congress directed the Commission to take account of changes in technology and economics in applying the standards of the Act. Section 2(a)(29)(A) directs the Commission to "consider[] the state of the art" in determining whether a public utility system is properly integrated. The Commission and the courts have recognized the need to consider a proposed transaction "in the light of contemporary circumstances . . . and of our present view of the Act's requirements," as well as to the need to "refashion[] . . . from time to time" the Act's "system of pervasive and continuing economic regulation . . . to keep pace with changing economic and regulatory climates."[21] Accordingly, the Commission should not hesitate to recognize the impact of

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[20] *American Natural Gas Co.*, 43 S.E.C. 203 (1966), the other case specifically cited by the Court, does not present the type of analysis suggested by the Court's dicta. There, the Commission stopped short of finding all five states bordering on the Great Lakes as a single distinct region but noted that the principal cities served by the acquired company were closer to the headquarters of the one of the acquirer's two current subsidiary operating companies than was the principal city served by the other operating subsidiary. Based on that fact, it found that the post-acquisition company would be confined to a single area or region. 43 S.E.C. at 206. The case did not turn on a discussion of "common geographic and geologic traits," or "identified similarities between the areas currently served" by the merging companies.

[21] *Union Electric Co.*, 45 S.E.C. 489, 503 & n.52 (1974), *aff'd without opinion sub nom. City of Cape Girardeau v. SEC*, 521 F.2d 324 (D.C. Cir. 1975). *See Connecticut Yankee Atomic Power Co.*, 41 S.E.C. 705, 710 (1963) (finding the "single area or region" requirement met "in view of the existing state of the arts of generating and transmission and the demonstrated economic advantages of the proposed arrangement[].''); *American Electric Power Co., Inc.*, 46 S.E.C. 1299, 1309-10 (1978) (noting that technological developments between 1946 and 1978,

changes in engineering and technology – or the policies of other regulators, such as the FERC – on its determination of whether a system satisfies the "single area or region" requirement.[22] These changes in the electric industry could properly be found to overshadow the considerations that the Commission cited nearly 60 years ago in its *Middle West* orders, such as "common geographic or geologic traits."

Second, Section 2(a)(29)(A) must be interpreted as a whole and in light of the overall purposes of the Act.[23] While the Commission (absent a major change in its interpretation of the Act) must give independent weight to the "single area or region" requirement, it remains true that evidence that supports one requirement may also be relevant to and support other requirements.[24] Without discounting the Court's conclusion that independent findings are required in connection with "a single area or region," the Commission was correct that its findings under other provisions of the Act are relevant to the question of "single area or region", including the finding of over $2 billion in savings from efficiencies resulting from the Merger.

In light of these considerations, the Order correctly found that the Combined System would be confined in its operations to a single area or region but did not fully articulate the reasons that support the finding. As explained in the sections that follow, AEP will present evidence to support the Commission's prior finding that the Combined System is located in a "single area or region," as required by Section 2(a)(29)(A). The evidence will support the analysis suggested by the Court's *dicta*,

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including the increased size of generating units and improved transmission of electricity over greater distances, justified larger systems than had been permitted in earlier years); *see also Mississippi Valley Generating Co.*, 36 S.E.C. 159, 186 (1955) ("Congress did not intend to impose rigid concepts but instead expressly included flexible considerations," including the statutory references to "the state of the art and the nature of the area or region affected, factors that are in their very nature conceived of as involving changing conditions and requiring individual examination.").

[22] In other contexts, the Commission and the courts have deemed it appropriate for the Commission to look to the FERC for its expertise in resolving anticompetitive operational issues. *Northeast Utilities*, Holding Co. Act Release No. 25273, 50 S.E.C. 511 (Mar. 15, 1991), *aff'd sub nom. City of Holyoke Gas & Electric Department v. SEC*, 972 F.2d 358 (D.C. Cir. 1992).

[23] *See Dole v. United Steelworkers*, 494 U.S. 26, 35 (1990) ("[I]n expounding a statute, we are not guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy.").

[24] *See WPL Holdings, Inc.*, Holding Co. Act Release No. 25377, 50 S.E.C. 728 (Sept. 18, 1991) (explaining that "some overlap of the analyses under section 10(c)(1) and 10(c)(2) is inevitable"; rather than "double counting," such overlap is "an incident of the application of a broad and comprehensive statute to the specifics of this particular situation"); *Entergy Corp.*, 51 S.E.C. 869, 876 n.35, citing *WPL Holdings* ("the Act repeats certain requirements in various statutory provisions to ensure complete supervision over the development of holding company systems"); *Commonwealth & Southern Corp.*, Holding Co. Act Release No. 7615, 26 S.E.C. 464 (Aug. 1, 1947) ("We do not, in applying particular size standards, lose sight of the objectives of other criteria. There must be a reconciliation of all objectives to the end of accomplishing a satisfactory administration of the Act.").

focusing on both common economic characteristics of AEP's region, and other factors that tend to unify and identify the region, making it distinct.

b. Common Characteristics of AEP's Area of Operations.

The Commission has traditionally approached the "single area or region" requirement through case-by-case determinations in which it looks to the particular characteristics of the areas in which the merging electric systems will operate, and considers whether the Combined System will be integrated in light of economic, geographic, demographic, or other relevant characteristics, such that it should be deemed to operate in a "single area or region" for purposes of the Act. The Commission has not insisted that any particular characteristics be present to support such a finding but rather has looked to all of the evidence present in each case, and has tailored its findings to the facts and circumstances of the particular applicants.

Applying this standard to the case at hand, the Commission can conclude that the Combined System is confined in its operations to a "single area or region," based on any one of the four independent rationales discussed below, which are presented by AEP as alternative contentions.

i. The Combined System is part of a larger single area or region as demonstrated by trade flows and infrastructure

AEP will present evidence to establish that the Combined System is part of a larger single area or region as demonstrated by trade flows and infrastructure. The infrastructure is comprised of road networks, waterways, pipelines, telecommunications systems and other facilities that have developed considerably over the past 70 years to lower the cost of both transportation and communications and to facilitate trade within the region. The significant trade flows illustrate the linkages among parts of the region. AEP will provide information regarding the concepts developed by regional economists and economic geographers to explain regional development and the importance of transportation linkages and resulting trade flows. AEP will provide descriptions of the infrastructure and relevant data, including maps, geological considerations, infrastructure capacities and activities, commodity price information, and trade flows. This overall set of information demonstrates that the Combined System operates within a single larger region with significant internal linkages.

ii. The Eastern Interconnection is a distinct region from an electricity perspective and the Combined System is primarily confined in its operations to the Eastern Interconnection.

AEP will present evidence to demonstrate that, as a result of engineering developments and the construction of transmission lines in the United States since the passage of the Act, the electric utility industry today is divided into three major electricity interconnections – the Eastern Interconnection, the Western Interconnection and the Electric Reliability Council of Texas ("ERCOT")[25]. In contrast, when the Act was passed, electricity could be transmitted only within more narrowly confined geographic areas. Most power was consumed within 15 to 25 miles from the point of generation and the maximum range for transmission of power was around 300 miles, which was uncommon. *See* Testimony of ICC Commissioner Walter M. W. Splawn, Hearings Before the Senate Committee on Interstate Commerce at 75-76 (April 16, 1935); *see also id.* at 85 (a company's service area "has to be small, because they cannot send power very far"). Today, however, as the Commission observed in approving the Merger, "a geographic radius of 1,000 miles or more is currently considered reasonable for choosing among supply options." Order at 60.

In view of the advances in generation and transmission technology, factors that might have constrained the size of the geographic area or region in which utilities could operate efficiently and reliably as a single, integrated system 60 years ago are no longer present, and the definition of a single region or area should take the current realities into account. Because of the greater degree of interconnection and electrical interdependence in the industry, these technological facts are more significant in identifying a single area or region than the factors relied upon by the Commission in cases decided shortly after the Act was passed.

The United States Supreme Court, in its recent decision upholding FERC Order No. 888, noted that:

> unlike the local power networks of the past, electricity is now delivered over three major networks, or "grids" in the continental United States . . . [A]ny electricity that enters the grid immediately becomes a part of a vast pool of energy that is constantly moving in interstate commerce. As a result, it is now possible for power companies to transmit electric energy over long distances at a low cost.

[25] *See* Attachment A, a map illustrating the three interconnections.

New York v. FERC, 535 U.S. 1, 7-8 (2002) (footnotes omitted). The Supreme Court thus recognized the very point that the Commission has emphasized in its prior cases, namely, technological developments extending the geographical range within which electric power may be physically transmitted are a relevant consideration in applying the "single area or region" test.[26]

These grids, or "interconnections," are significant, for present purposes, because they mean that different facilities located within an "interconnection," even if not contiguous or directly interconnected, are part of the same electric transmission system. As FERC has emphasized, through "interconnections," the "transmission facilities of any one utility in a region are part of a larger, integrated transmission system." In terms apt for the Commission's present purpose of determining whether AEP's operations are within a "single" area or region, like the U.S. Supreme Court, FERC has emphasized that:

> From an electrical engineering perspective, each of the three interconnections in the United States (the Eastern, the Western, and ERCOT) operates as a single machine.

Regional Transmission Organization, Notice of Proposed Rulemaking, IV FERC Stats. & Regs. ¶ 32,541 at 33,697.

All of AEP's non-ERCOT operations are entirely within the Eastern Interconnection and, as has been described, are clearly within a single area or region for purposes of the Act. AEP's ERCOT operations are necessarily within the same area or region as the AEP operations within the Southwest Power Pool ("SPP") (originally a reliability council and currently an RTO located in the southwest portion of the Eastern Interconnection). *See Central and South West Corp.*, Holding Co. Act Release No. 22439 (Apr. 1, 1982). In that proceeding, certain parties had challenged whether CSW was in compliance with the integration standards of the Act as a result of its utility operations being partly situated in SPP and partly situated in ERCOT. *Id.* at 3. At that time SPP and ERCOT were two separate reliability councils that had no interconnection between them. The Commission dismissed the proceedings on the grounds that CSW had promised to build two interconnections (one of which was to be a joint effort with unaffiliated utilities) between its SPP and ERCOT operations. *Id.* at 9. The interconnections were subsequently built and are currently used by AEP to integrate the operations of the Combined System. The Commission found the CSW's utility operations in SPP and ERCOT to be integrated (and implicitly within a single area or region) on the basis of such interconnection in 1982; therefore, it follows that they are

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[26] As noted previously, in the *Connecticut Yankee Atomic Power Company* case, for example, the Commission emphasized the "existing state of the arts of generating and transmission" in finding that "each sponsor may be considered to operate in the same area or region." 41 S.E.C. 705, 710 (Nov. 15, 1963); *see also, e.g., Vermont Yankee Nuclear Power Corp.*, 43 S.E.C. 693 (Feb. 6, 1968) (same).

still in a single area or region today.

iii. *The area consisting of contiguous Regional Transmission Organizations with either existing or contemplated robust Joint Operating Agreements is a distinct region and the Combined System is primarily confined in its operations to this Region.*

Since at least the passage in 1935 of the Act and its companion, Part II of the Federal Power Act, federal government policy has encouraged and promoted the increasing interconnection and coordination of electric utilities. As a result of this policy and improvements in technology, the electric industry has become increasingly interconnected and interdependent. The practical result has been to greatly expand the concept of a single area or region.

In recent years, FERC has pursued a policy of expanding the scope and scale of electric industry institutions and markets. FERC's underlying objectives have been promotion of increased competition and enhancement of reliability. AEP will present testimony to explain the development of these policy initiatives, which were well underway at the time the Commission approved the Merger. They can be divided roughly into three phases.

The first phase began with FERC Order No. 888, which, as discussed earlier, essentially made interstate transmission systems common carriers. This action, by itself, greatly expanded the interaction of electric utilities and use of the interstate transmission grid. Electric transmission systems, which once were used principally by vertically-integrated electric utilities to serve their local customers, became increasingly used for commerce between and among utilities. New industry entrants, including independent power producers or Exempt Wholesale Generators ("EWGs") and power marketers, began to use electric transmission systems to effect long distance power transactions. FERC has described the effect of Order No. 888 (and its companion order, No. 889), as follows:

> Power resources are now acquired over increasingly large regional areas, and interregional transfers of electricity have increased.
>
> The very success of Order Nos. 888 and 889, and the initiatives of some utilities that have pursued voluntary restructuring beyond the minimum open access requirements,

have placed new stresses on regional transmission systems – stresses that call for regional solutions.[27]

The "regional solutions" fashioned by FERC included its issuance of Order No. 2000 on December 20, 1999, signaling the second phase of its policy initiatives. FERC issued Order No. 2000 to advance the formation of RTOs. In that order, FERC stated that it was its objective for all transmission-owning entities in the nation to place their transmission facilities in the control of appropriate RTOs. RTOs must be of adequate "scope and configuration", which means that they must include many utilities and cover a large geographical area. FERC's model of an appropriate RTO is one that not only functionally controls the combined transmission systems of multiple electric utilities, but also centrally dispatches the generation resources in the RTO on a bid basis, and operates electricity markets within its boundaries.

Since Order No. 2000, several RTOs have been approved by the FERC, including PJM Interconnection, L.L.C. ("PJM"), the Midwest Independent System Operator, Inc. ("MISO") and SPP. These three very large RTOs cover the area encompassed by the Combined System (excluding ERCOT) and beyond.[28] In fulfillment of conditions imposed by the FERC on approval of the Merger, AEP's east zone operating companies have become members of PJM and its non-ERCOT west zone companies are members of SPP.

The third phase of FERC's policy initiatives began with its issuance of a Notice of Proposed Rulemaking proposing a Standard Market Design for the nation ("SMD NOPR").[29] Among other things, the SMD NOPR envisioned the creation of huge electricity markets, employing centralized dispatch of generation resources, and tying together RTOs through joint operating agreements and joint and common markets.

In July 2002, FERC conditionally approved the choice of AEP and others to join the PJM RTO instead of MISO but imposed conditions that emphasized FERC's

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[27] *Regional Transmission Organizations*, Order No. 2000, 65 Fed. Reg. 809 (Jan. 6, 2000) FERC Stats. & Regs. ¶31,089, at 30,997-98 (2000), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (Feb. 25, 2000), FERC Stats. & Regs. ¶31,092 (2000), *aff'd sub nom. Public Utility District No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (DC Cir. 2001)("Order No. 2000").

[28] *See* Attachment B, a map showing the PJM, MISO and SPP RTOs and ERCOT.

[29] *Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design*, Notice of Proposed Rulemaking, 67 Fed. Reg. 55,452 (Aug. 29, 2002), FERC Stats. & Regs. ¶ 32,563 (2002).

desire to bring PJM and MISO together into one huge energy market.[30] As a result, the practice of charging additive transmission rates for transactions within the combined PJM/MISO will be eliminated, effective December 1, 2004. The MISO/PJM joint operating agreement ("JOA") has been negotiated and accepted by FERC and is now in operation. The JOA is a state-of-the-art agreement providing for a higher level of operational coordination and cooperation than had ever existed between or among existing RTOs, utilities or control areas. The MISO/PJM joint and common market is under development.

As large as this market is, it will become even larger, encompassing the SPP as well, as the result of orders issued in 2004 by FERC granting SPP RTO status.[31] FERC conditioned that acceptance upon SPP's creation of a joint and common market with MISO and negotiation of a JOA between SPP and MISO. FERC has accepted a JOA addressing early stage ("non-market to non-market") operations and has ordered SPP and MISO to negotiate and file a mutually agreeable JOA for more advanced ("market to non-market") operations by December 1, 2004.[32]

The above described FERC actions will tie the east and west zones of AEP together as part of the huge electricity coordination and market area encompassed by PJM, MISO and SPP. Once SPP and MISO adopt a JOA, the region consisting of PJM, MISO and SPP will become an economically distinct and identifiable area or region in which electricity may be transacted with minimal transactional impediments. With respect to transmission tariffs, that region will resemble a customs union. It is expected that these actions will result in fewer variations in the wholesale price of electricity, increased wholesale activity and more efficient distribution of energy resources. These actions make it very clear that from the standpoint of FERC policy, the Combined System lies within a single area or region.

The operations of the Combined System will be primarily confined to this distinct area or region. All of AEP's non-ERCOT operations will be entirely within this region and therefore confined to a "single area or region" for purposes of the Act. For purposes of analysis of this contention under the Act, the ERCOT portion of TNC and TCC, located exclusively in ERCOT, is necessarily within the same area or region by

[30] *Alliance Companies*, 100 FERC ¶ 61,137 (2000), *order on clarification*, 102 FERC ¶ 61,214, *order on reh'g and clarification*, 103 FERC ¶ 61,274, *order denying reh'g and granting clarification*, 105 FERC ¶ 61,215 (2003) (Nov. 17, 2003 Order), *appeal docketed sub nom. American Electric Power Serv. Corp. v. FERC*, No. 03-1223 (D.C. Cir. Aug. 1, 2003).

[31] *Southwest Power Pool, Inc.* 106 FERC ¶ 61,110 (2004); *order on compliance filing*, 108 FERC ¶ 61,003 (2004).

[32] *Southwest Power Pool, Inc.* 109 FERC ¶ 61,108 (2004).

virtue of the Commission's findings in *Central and South West Corp.,* Holding Co. Act Release No. 22439 (Apr. 1, 1982), for the reasons set forth in the preceding section.

iv. The Area of the Combined System's First-Tier Interconnected Utilities Defines a Single Region in Which the Combined System Operates.

The Commission has defined relevant energy regions by application of the concept of the service areas of "first-tier utilities." The "first-tier utilities" are the merger applicants and all utilities interconnected with either or both merger applicant. While the Commission developed the approach of defining first-tier utilities as the merged company's region in the context of applying Section 10(b)(1) of the Act, which looks to the potential effects of a proposed merger on competition within the region, it is also relevant to applying the "single area or region" test under Section 10(c)(1). *See Northeast Utilities*, Holding Co. Act Release No. 25221 (Dec. 21, 1990) ("Section 10(b) allows the Commission to exercise its best judgment as to the maximum size of a holding company in a particular *area*, considering the state of the art and the *area or region* effected") (emphasis added).[33] In other words, two separate criteria under the Act require the Commission to identify the relevant area or region of the resulting entity when approving a merger. It follows that the area or region identified by the Commission under one criterion can be the same area or region for purposes of the second criterion. Because the resulting area is one mass rather than two, the service territories of the first-tier utilities interconnected with AEP and CSW constitute a "single area or region" in satisfaction of that test. See Attachment C. Conversely, a map of the first tier utilities of two distant utilities would result in two distinct masses, not one.

Section 10(b)(1) of the Act requires the Commission to examine whether a proposed acquisition "will tend towards . . . the concentration of control of public-utility companies, of a kind detrimental to the public interest or the interest of investors or consumers." The Commission has used its authority under Section 10(b)(1) to examine the effect of the size of the merged company, as well as the effects of the merger on competition. To analyze the effect of the size of a merger under Section 10(b)(1), the Commission has examined, in particular, the size of the merged entity relative to its "region." This analysis requires identification of the relevant "region" with respect to each merger.

In its 1993 order approving Entergy Corporation's proposed acquisition of Gulf States Utilities, the Commission adopted and approved Entergy's proposal that the appropriate region for this 10(b)(1) test be defined by the first-tier interconnections of the

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[33] *See, e.g., Sierra Pacific Resources,* Holding Co. Act Release No. 24566, 49 S.E.C. 735 (Jan. 28, 1988); *Eastern Utilities Associates*, Holding Co. Act Release No. 24245 (Nov. 21, 1986).

merging companies (that is, the relevant region consisted of the Entergy and Gulf States operating territories, and all the utilities interconnected with either). Analyzing the competitive effects of the merger in light of this definition of the relevant region, the Commission found that the merger "would not significantly change the relationship between the size of the Entergy system and the rest of the electric utility industry in the region."[34] AEP also used the "first-tier utility" method to define the relevant region under Section 10(b)(1) in its application. The Commission found that the Merger satisfied the requirements of Section 10(b)(1), and that finding was not challenged on appeal.

In so holding, the Commission emphasized that under Section 10(b)(1), it is called upon to "exercise its best judgment as to the maximum size of a holding company in a particular *area*, considering the state of the art and the *area or region* affected."[35] As this statement shows, this function is analogous to the nature of the Commission's inquiry in determining whether the system will operate in a "single area or region." While the objectives of the two inquiries are different (in the first case to assess whether the merged company would unduly dominate business in the area or region in which it operates, in the second to determine whether the merged company would operate in a single area or region), in both cases the Commission must decide how to delineate the "area or region" in which the merged company will operate. Indeed, the Commission has acknowledged that the inquiry under Section 10(b)(1) is related to the analysis of whether a utility is an "integrated public-utility system." In *Entergy*, the Commission cited Section 2(a)(29), the definition of an "integrated public-utility system," in support of the proposition that the Commission must "exercise its best judgment under Section 10(b)(1) as to the maximum size of a holding company in a particular area."[36]

It makes sense under the statute to apply the same standard for the single area or region test under Section 10(c)(1). Utilities operate in an increasingly competitive and interconnected environment. A determination of whether a merged utility will operate in a "single area or region" should begin with the recognition that the merger entity will not operate in isolation, but will interact with other utilities, particularly those that it can reach most economically – *i.e.*, those with which it is directly interconnected. It is precisely for that reason that FERC looks at interconnected utilities as the most

[34] *Entergy Corp.*, Holding Co. Act Release No. 25952 (Dec. 17, 1993), *reconsideration denied*, Holding Co. Act Release No. 26037 (Apr. 28, 1994), *remanded sub nom. Cajun Elec. Power Coop. Inc. v. SEC*, 1994 WL 704047 (D.C. Cir. Nov. 16, 1994), *on remand, Entergy Corp.*, Holding Co. Act Release No. 26410, 52 S.E.C. 481 (Nov. 17, 1995) (citations omitted) (emphasis added).

[35] *Entergy Corp.*, Holding Co. Act Release No. 25952 (Dec. 17, 1993) (quoting *Centerior Energy Corp.*, Holding Co. Act Release No. 24073 (Apr. 29, 1986)) (emphasis added). *See also American Electric Power Company, Inc.*, 46 S.E.C. 1299, 1309 (1978).

[36] *Entergy Corp.*, Holding Co. Act Release No. 25952 at n.34 (Dec. 17, 1993).

relevant markets for its horizontal antitrust analysis.[37] Thus, it is useful to look to *Entergy's* recognition of the "first-tier utility" method as an appropriate way of defining the "region" for purposes of the Act's Section 10(b)(1) analysis, since the same concept is equally valid for purposes of applying the "single area or region" standard. This "first-tier utility" method of defining the relevant "region" as endorsed by the Commission in *Entergy* shows that that the Combined System is in a single area or region.

Attachment C is a map showing that AEP, CSW and their first-tier utilities are in a single region. The shaded area on the map forms a single seamless area, devoid of any attributes of uneconomical gerrymandering or "scatteration." As further indicated on the map, this area or region has a well-developed transmission system that interweaves and binds together this region and supports its function as an interconnected economic unit. This evidence shows, in sharp visual effect, that under the "first-tier utility" method as well, the area in which AEP operates is confined to a "single area or region."[38] AEP will present testimony to sponsor Attachment C.

[37] FERC's guidelines for the review of electric utility mergers provide further support for this conclusion, suggesting independently the same concept of the bounds of the market likely to be affected by a merger. The FERC requires that merger applicants submit a detailed quantitative analysis that covers the merging firms and all directly interconnected electric systems and service areas. *Revised Filing Requirements Under Part 33 of the Commission's Regulations*, Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,878-9 (2000); *order on reh'g*, Order No. 642-A, 94 FERC ¶ 61,289 (2001). In reviewing the AEP-CSW merger, FERC found that the applicants' use of directly interconnected customers (and some historical customers) as relevant destination markets was in accordance with FERC's Merger Policy Statement). *See American Elec. Power Co. and Central and South West Corp.*, Opinion No. 442, 90 FERC ¶ 61,242 at 61,780 (2000), citing *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, FERC Stats. & Regs. ¶ 31,044 at 30,119 (1996); *order on reconsideration*, Order No. 592-A, 79 FERC ¶ 61,321 (1997).

[38] This approach can also be used to addresses the question raised by the Court concerning the length of the contract path and the implications for "single area or region."

Conclusion

The foregoing discussion identifies four well-supported rationales, any one of which fully justifies the conclusion that the merged AEP is a system confined to a single area or region of the United States.

Respectfully submitted,

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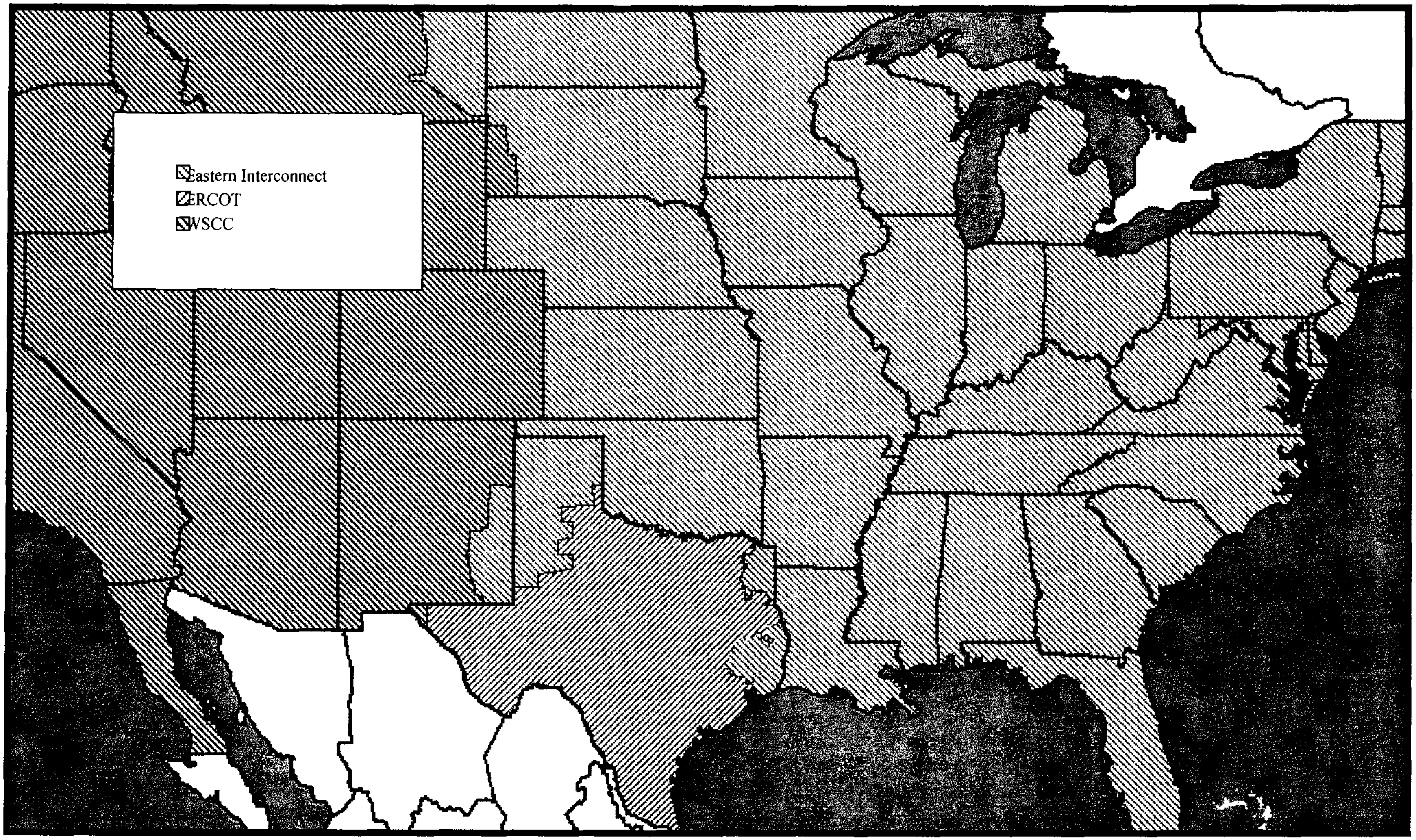
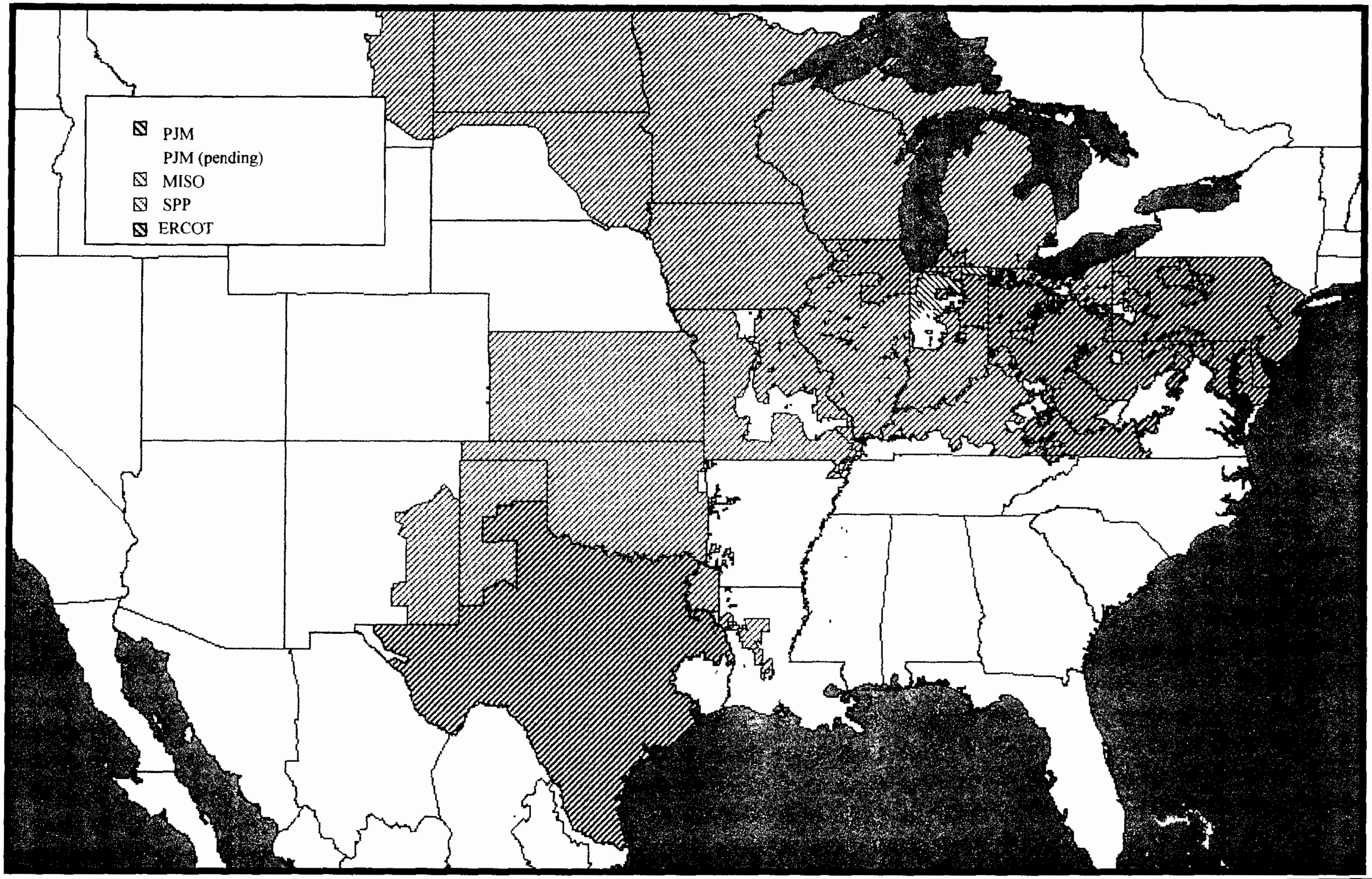
Attachment A



Attachment B



Attachment C